

DEPARTMENT OF STATE REVENUE

Revenue Ruling #IT 99-01

March 25, 1999

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUE

Adjusted Gross Income Tax and Supplemental Net Income Tax – Sale of the Stock of a Subsidiary by the Parent

Authority: IC 6-3-1-3.5, IC 6-3-1-11, IC 6-3-8, IC 6-3-1-20, IC 6-3-2-2, Rule 45 IAC 3.1-1-50

The taxpayer (parent) requests the Department to rule on the treatment of the sale of the stock of a subsidiary by the taxpayer. The taxpayer submitted the following statements in relation to this request for Departmental review.

1. The taxpayer's sale of the stock of a subsidiary in 1998 will be ignored.
2. The taxpayer's group will report the gain from the subsidiary's deemed asset sale as apportionable business income for adjusted gross income tax and supplemental net income tax purposes.
3. Pursuant to IC 6-3-2-2(l) and/or Regulation 45 IAC 3.1-1-62, the taxpayer's group may exclude all receipts from the subsidiary's deemed asset sale (and the stock sale by the taxpayer) from the numerator and denominator of the taxpayer's group's sales factor.

STATEMENT OF FACTS

The taxpayer's former subsidiary operates a production facility in Indiana. It, also, holds other assets located both inside and outside of Indiana. Until 1998 the subsidiary was wholly owned by the taxpayer. In 1998 the taxpayer sold all of its stock in the subsidiary. An election will be made by the parties to treat the stock sale as an asset sale

by the subsidiary under Internal Revenue Code Section 338(h)(10), i.e., the gain on the sale of the stock by the taxpayer will be ignored, but, the gain on the subsidiary's deemed sale of its assets will be included in the taxpayer's group's consolidated adjusted gross income.

For the 1998 tax year, the taxpayer's group will file a consolidated adjusted gross income tax return including the subsidiary for the appropriate short period. The taxpayer's group uses one consolidated apportionment factor to apportion the group's business income to Indiana. For the two years prior to 1998, the Indiana sales factor for the taxpayer's group averaged approximately 11% (or 22% when double-weighted). The estimated sales factor for 1998 for the taxpayer's group is about 13% (26% when double-weighted) without reflecting the Internal Revenue Code Section 338(h)(10) transaction. If, for example, the so-called modified aggregate deemed sale price as calculated under Internal Revenue Code Section 338(h)(10) and related regulations was required to be reflected in both the sales factor numerator and denominator, that factor could increase over 300%.

STATEMENT #1 – DISCUSSION

Pursuant to IC 6-3-1-3.5 and IC 6-3-1-11, Indiana corporate adjusted gross income tax is based on Internal Revenue Code Section 63 "taxable income" with certain modifications. This being the case, for adjusted gross income tax and supplement net income tax (IC 6-3-8) purposes, the taxpayer's sale of the stock of its subsidiary in 1998 will be ignored, but, the gain on the taxpayer's subsidiary's deemed sale of its assets will be included in the taxpayer's group's consolidated adjusted gross income.

STATEMENT #1 – RULING

The Department rules that the taxpayer's sale of the stock of its subsidiary in 1998 will be ignored, but, the gain on the subsidiary's deemed sale of its assets will be included in the taxpayer's group's consolidated adjusted gross income for adjusted gross income tax and supplemental net income purposes.

STATEMENT #2 – DISCUSSION

IC 6-3-1-20 provides:

The term "business income" means income arising from transactions and activity in the regular course of the taxpayer's trade or business and includes income from tangible and intangible property if the acquisition, management, and disposition of the property constitutes integral parts of the taxpayer's regular trade or business operations.

In the instant case, the gain from the subsidiary's deemed asset sale falls within the ambit of IC 6-3-1-20, therefore, the gain is defined as apportionable "business income".

STATEMENT #2 – RULING

The Department rules that the taxpayer's group may report the gain from the subsidiary's deemed asset sale as apportionable business income for adjusted gross income tax and supplemental net income tax purposes.

STATEMENT #3 – DISCUSSION

IC 6-3-2-2(l) states:

If the allocation and apportionment provisions of this article do not fairly represent the taxpayer's income derived from sources within the State of Indiana, the taxpayer may petition for or the department may require in respect to all or any part of the taxpayer's business activity, if reasonable:

1. separate accounting;
2. the exclusion of one (1) or more of the factors;
3. the inclusion of one (1) or more additional factors which will fairly represent the taxpayer's income derived from sources within the State of Indiana; or
4. the employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income.

Rule 45 IAC 3.1-1-50, interpreting IC 6-3-2-2(l), provides that "In some cases, certain gross receipts should be disregarded in determining the sales factor to effectuate an equitable apportionment." Here, the inclusion of the receipts from the deemed sale of assets by the taxpayer's subsidiary in the taxpayer's group's sales factor distorts the sales factor, hence, the taxpayer's group's income derived from Indiana is not fairly represented.

STATEMENT #3 – RULING

The Department rules that the taxpayer's group may exclude all receipts from the taxpayer's subsidiary's deemed asset sale (and the stock sale by the taxpayer) from the numerator and denominator of the taxpayer's group's sales factor.

CAVEAT

This ruling is issued to the taxpayer requesting it on the assumption that the taxpayer's facts and circumstances, as stated herein, are correct. If the facts and circumstances given are not correct, or if they change, then the taxpayer requesting this ruling may not rely on it. However, other taxpayers with substantially identical factual situations may rely on this ruling for informational purposes in preparing returns and making tax decisions. If a taxpayer relies on this ruling and the Department discovers, upon

examination, that the fact situation of the taxpayer is different in any material respect from the facts and circumstances given in this ruling, then the ruling will not afford the taxpayer any protection. It should be noted that subsequent to the publication of this ruling, a change in a statute, regulation, or case law could void the ruling. If this occurs, the ruling will not afford the taxpayer any protection.

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